



CITY OF LODI

COUNCIL COMMUNICATION

AGENDA TITLE: COMPREHENSIVE ANNUAL FINANCIAL REPORT & SINGLE AUDIT
(FISCAL YEAR 1995-96)

MEETING DATE: November 20, 1996

PREPARED BY: Finance Director

RECOMMENDED ACTION: That the City Council receive for file the following reports and financial statements submitted by KPMG Peat Marwick LLP and the Finance Department for Fiscal Year 1995-96.

- The Combined Annual Financial & Single Audit Report
- The Management Letter
- The SAS 61 Report (Report to City Council)

BACKGROUND INFORMATION: The annual audit was conducted to ensure the City Council and other interested parties that the City's financial records and reports are prepared in accordance with generally accepted accounting principles (GAAP), that internal controls are adequate and protect the City against loss from unauthorized use or disposition and that the City has complied with all agreements and covenants to obtain grant funds and debt financing. KPMG Peat Marwick has issued an "unqualified opinion". KPMG Peat Marwick auditors will be in attendance at the meeting.

When the printing of the Financial Statements is finalized, these reports will be provided to Federal and State oversight agencies, bond trustees and insurance companies for their review and evaluation. Copies of the reports were provided to the City Council under separate cover. An information copy of the Combined Annual Financial & Single Audit report will be available during the Council meeting. A copy of the report may be requested by the public by contacting the Finance Department Accounting Manager. Copies will be mailed out as soon as they are received from the printer.

Certificate of Achievement

The City received a Certificate of Achievement for Excellence in Reporting from the Government Finance Officers Association (GFOA) and the California Society of Municipal Finance Officers (CSMFO) for the third year in a row. Copies of these certificates are included in the 1995-96 Financial Report.

Acknowledgments

Ruby Paiste, Audrey Mathers and Cory Wadlow of the Accounting section of the Finance Department are to be commended for their hard work and professionalism in preparing the City's Annual Financial Reports. It is due to their dedication to excellence and to the City that Lodi has been recognized by the auditors and other finance professional organizations.

FUNDING: None


Vicky McAthie
Finance Director

APPROVED:


H. Dixon Flynn -- City Manager



Peat Marwick LLP

400 Capitol Mall
Sacramento, CA 95814

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November 15, 1996

The Honorable Members of the City Council
City of Lodi, California:

We have audited the general purpose financial statements of the City of Lodi (the City) for the year ended June 30, 1996, and have issued our report thereon dated October 4, 1996. In planning and performing our audit of the general purpose financial statements of the City, we considered the internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the general purpose financial statements and not to provide assurance on the internal control structure. We have not considered the internal control structure since the date of our report.

During our audit we noted certain matters involving the internal control structure and other operational matters that are presented for your consideration. The following comments and recommendations, all which have been discussed with the appropriate members of management, are intended to improve the internal control structure or result in other operating efficiencies and are summarized as follows:

Participation in Joint Ventures

The City, in the normal course of operation, participates in a number of joint ventures in which oversight responsibility has been established. One of the joint ventures, Northern California Power Agency (NCPA), has various agreements and obligations that have a potential effect on the City's financial position, including general debt commitments and individually financed operating plants, projects and programs. We understand that in order to fund these foreseeable obligations as well as contingent liabilities that are not budgeted but may require significant future expenditures, Members of the NCPA have established a general operating reserve. As of June 30, 1996, the City had a balance of approximately \$17.3 million in the NCPA General Operating Reserve. This asset and the related obligations and contingent liabilities are recorded in the NCPA's financial statements and are disclosed but not recorded in the City's financial statements. Activity is monitored by City management through representation on the NCPA's Commission.



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The Honorable Members of the City Council
November 15, 1996
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We recommend that the City and the Electric Utility Department develop a policy, in conjunction with their strategic plan for deregulation of the electric industry, as to the appropriate level of funding that is required to be on deposit with the NCPA for further obligations and contingent liabilities and procedures for the use of such funds. In addition, the City should evaluate on a periodic basis the investment policies underlying collateral and the risks associated with maintaining a general operating reserve with the NCPA in accordance with the City's established investment policies.

Grant Administration

During the audit, we noted that the application for Transportation Development Act (TDA) funds was not filed in a timely manner, resulting in a delay in grant funding.

We recommend that when the City makes initial application for such funds that the Finance Department Revenue Manager be advised as to the frequency and expected filings that will be made in order to properly monitor the timely receipt of such funds.

Accounting for Recreation Activities

During our review of the internal controls, we noted that the Parks and Recreation Department collects registration fees for and on behalf of several sporting activity organizations. We understand that many of these organizations significantly benefit the City and the citizens of Lodi. The City, however does not control or direct such organization's actions. It is our understanding that there is no formal documentation which clarifies or limits the responsibility of the City with respect to these activities or the services that are provided for such organizations.

We recommend that the City evaluate the need to document and formally communicate the specific services it will provide to such organizations and thereby limit the exposure of the City to potential litigation. As part of these services, the City should develop specific procedures whereby the Parks and Recreation staff reconcile the registration forms received for non-City sponsored programs to the funds actually received.

Library Investments

During the audit, we noted that the Library fund has several stock investments held in a trust account that were donated by private individuals several years ago for and on behalf of the Library. Although these investments have experienced significant appreciation during the past several years, stock investments are currently not within the guidelines of the City's adopted investment policy or general governmental investment policies due to their speculative nature and volatility of the stock investment markets.

We recommend that the Library Board and the City develop a policy and procedures for donated property and investments that will ensure that the City is within established guidelines for investments.

Risk Management and Self Insurance

As noted over the past years, risk management and self insurance has been an area that requires significant judgment and estimation of liabilities. As we understand, the City has recently appointed a new Risk Manager to monitor the City's self insurance programs.

We recommend that the City develop a policy for the required level of funding for the self insurance fund and develop procedures for the allocation of those costs associated with administering such a program on an equitable basis that takes into consideration the inherent risks and exposures of the activities of each department. In addition, the Risk Manager should work closely with the City Attorney in determining overall risks and exposure to contingent liabilities by the City and ensure that proper reserves are established.

Changes in Single Audit Requirements

The *Single Audit Act Amendments of 1996* became effective on July 1, 1996. The Act raises the threshold for entities subject to the Act's requirements to \$300,000 from \$25,000. The new act makes significant changes to the concept of a major program. Previously, the distinction between major and nonmajor programs was based entirely on a dollar amount. The new act takes a risk-based approach, giving the office of Management and Budget (OMB) Director discretion to prescribe the implementation criteria. Auditors must classify a sufficient number of program as major to ensure that at least 50 percent of federal expenditures are covered by their audit.

In response to complaints from federal and state program managers that single audit reports contain too many subreports to be useful and that the reports contained inadequate information on internal controls, the new act requires auditors to prepare a summary report regarding the audit entity's financial statements, internal controls, and compliance with laws and regulations.

The Honorable Members of the City Council
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Based upon the current level of federal financial assistance received by the City of Lodi, we anticipate that the City will continue to be subject to single audit requirements in fiscal year 1996-97 and beyond.

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Our audit procedures are designed primarily to enable us to form an opinion on the general purpose financial statements, and therefore may not bring to light all weaknesses in policies or procedures that may exist. We aim, however, to use our knowledge of the City's organization gained during our work to make comments and suggestions that we hope will be useful to you.

We would be pleased to discuss these comments and recommendations with you at any time.

This report is intended solely for the information and use of the City Council, management of the City and should not be used for any other purpose. This restriction is not intended to limit the distribution of this letter, which is a matter of public record.

Very truly yours,

KBRW Post Services LLP

CITY OF LODI, CALIFORNIA

Report to the City Council

Year Ended June 30, 1996



400 Capitol Mall
Sacramento, CA 95814

October 4, 1996

PRIVATE & CONFIDENTIAL

The Honorable Members of City Council
City of Lodi, California:

We have audited the general purpose financial statements of the City of Lodi, California for the year ended June 30, 1996, and have issued our report thereon dated October 4, 1996. Under generally accepted auditing standards, we are providing you with the attached information related to the conduct of our audit.

This information is intended solely for the use of the City Council and Management and should not be used for any other purpose.

KPMG Peat Marwick LLP



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Report of KPMG Peat Marwick LLP
to the City Council of the
CITY OF LODI, CALIFORNIA

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Our Responsibility Under Generally Accepted Auditing Standards

Our responsibility under generally accepted auditing standards is to express an opinion on the general purpose financial statements of the City of Lodi, California (City) based on our audit. In carrying out this responsibility, we assessed the risk that the general purpose financial statements may contain a material misstatement, either intentional or unintentional, and designed and conducted our audit to provide reasonable, not absolute, assurance of detecting misstatements that are material to the general purpose financial statements. In addition, we considered the internal control structure of the City to gain a basic understanding of the internal control policies and procedures in order to design an effective and efficient audit approach, not for the purpose of providing assurance on the internal control structure.

We have issued a management letter describing recommendations for improvements to the internal control structure of the City.

Significant Accounting Policies

The significant accounting policies used by the City are described in Note 1 to the general purpose financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year ended June 30, 1996.

We noted no transactions entered into by the City during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you of, or transactions for which there is a lack of authoritative guidance or consensus.

Management Judgments and Accounting Estimates

Accounting estimates are an integral part of the general purpose financial statements prepared by management and are based upon management's current judgments. Certain accounting estimates are particularly sensitive because of their significance to the general purpose financial statements and because of the possibility that future events affecting them may differ markedly from management's current judgments.

Management's estimate of the liability for self-insurance is based on an evaluation by a claims administrator for claims filed and management's evaluation of incidents incurred but not reported. While management uses the best information available to evaluate the adequacy of the liability, future adjustments may be necessary. We evaluate the key factors and assumptions used to develop the estimate in determining that the liability is reasonable in relation to the general purpose financial statements of the City taken as a whole.

Significant Audit Adjustments

There were no corrections to the general purpose financial statements that could, in our judgment, either individually or in the aggregate, have a significant effect on the City's financial reporting process.

Other Information in Documents Containing Audited Financial Statements

Our responsibility for other information in documents containing the City's general purpose financial statements and our report thereon does not extend beyond the financial information identified in our report, and we have no obligation to perform any procedures to corroborate other information contained in these documents. We have, however, read the other information included in the City's Comprehensive Annual Financial Report for the year ended June 30, 1996, and no matters came to our attention that cause us to believe that such information, or its manner of presentation, is materially inconsistent with the information, or manner of its presentation, appearing in the general purpose financial statements.

Disagreements with Management

There were no disagreements with management on financial accounting and reporting matters which, if not satisfactorily resolved, would have caused a modification of our report on the City's general purpose financial statements for the year ended June 30, 1996.

Consultation with Other Accountants

To the best of our knowledge management has not consulted with or obtained opinions, written or oral, from other independent accountants during the past year that were subject to the requirements of Statement on Auditing Standards No. 50, "Reports on the Application of Accounting Principles."

Major Issues Discussed with Management Prior to Retention

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the City's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing our audit.